United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

74-2405

United States Court of Appeals
For the Second Circuit

GERALD L. HERZFELD,
Plaintiff-Appellee,
—*against*—
LAVENTHOL KREKSTEIN HORWATH & HORWATH,
Defendant-Appellant.

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LAVENTHOL KREKSTEIN HORWATH & HORWATH,
Third-Party Plaintiff-Appellee,
—*against*—
ALLEN & COMPANY, INCORPORATED and
ALLEN & COMPANY,
Third-Party Defendants-Appellants.

P/S

ALLEN & COMPANY and ALLEN &
COMPANY, INCORPORATED,
Third-Party Counterclaimants-Appellants,
—*against*—
LAVENTHOL KREKSTEIN HORWATH & HORWATH,
Third-Party Counterclaim Respondent-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

**BRIEF OF
LAVENTHOL KREKSTEIN HORWATH & HORWATH
AS THIRD-PARTY
PLAINTIFF-APPELLEE and THIRD-PARTY COUNTERCLAIM
RESPONDENT-APPELLEE**

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Preliminary Statement

Laventhol Krekstein Horwath & Horwath ("Laventhol") is third-party plaintiff-appellee and third-party counterclaim respondent-appellee as to parts of the Amended Judgment (1129a* *et seq.*) rendered below by Judge Lloyd F. MacMahon in *Herzfeld* v. *Laventhol Krekstein Horwath & Horwath* ("*Herzfeld*"), 378 F. Supp 112 (S.D.N.Y. 1974). Laventhol is appellee as to those parts of the Amended Judgment which granted to Laventhol contribution in the amount of $76,500 to be mad by Allen & Company, Incorporated and Allen & Company (collectively "Allen") as against plaintiff's recovery in the amount of $153,000 from Laventhol. Additionally Laventhol is appellee with regard to the dismissal by the Court below of Allen's third-party counterclaims against Laventhol upon finding that Allen was *in pari delicto* with Laventhol.

It should be noted initially that should this Court find that the Court below erred in giving judgment to the plaintiff in the first place, for any of the reasons assigned in Laventhol's previously filed brief as defendant-appellant, the issues respecting contribution presented herein need not be reached by this Court.

Issues Presented

1. Did the Court below correctly decide that Laventhol's third-party claim against Allen for contribution for liability under Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, Section 352-c of the New York General Business Law, and the common law, was preserved by the federal and state law on contribution, notwithstanding Allen's prejudgment settlement with the plaintiff?

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* All references designated "a" are keyed to pages of the first four volumes of the Joint Appendix and all references designated "e" to pages of the last two volumes of the Joint Appendix.

2. Did the Court below correctly grant relief to Laventhol in the form of recovery for contribution in the amount of $76,500 with costs and interest to be paid by Allen on the ground that Allen was an active participant in any wrongdoing and thus should pay one-half of the amount of damages remaining due to the plaintiff?

3. Did the Court below correctly dismiss Allen's third-party counterclaims against Laventhol on the grounds that Allen was *in pari delicto* with Laventhol and had otherwise failed to prove its claims against Laventhol?

Proceedings Below

The complete factual setting in *Herzfeld* is fully set out in the brief of Laventhol as defendant-appellant previously filed with this Court. Nevertheless, certain facts are particularly pertinent to the discussion contained herein and are restated for the convenience of this Court.

The judgment entered below against Laventhol and in favor of the plaintiff allowed recovery in the amount of $153,000 with costs and interest but also gave recovery for contribution in favor of Laventhol as third-party plaintiff and against Allen in the amount of $76,500 with costs and interest and dismissed the third-party counterclaims of Allen.

Plaintiff Herzfeld brought this action against 12 defendants seeking recovery of $510,000 in damages suffered as a result of his purchase of securities of The Firestone Group, Ltd. ("Firestone Group") in a private placement managed by Allen (10a *et seq.*). Before the trial commenced, Allen negotiated a settlement with Herzfeld on behalf of itself and 10 other defendants, whereby plaintiff released all claims against those 11 defendants in return for payment of approximately $357,000 and expressly reserved any claims against Laventhol (62-64a). Over

Laventhol's objection that it had not been informed of the settlement negotiations and that it had cross claims for contribution and indemnification against the 11 defendants, the Court below nevertheless allowed the settlement. However, the Court allowed the settlement only upon the express reservation by the Court of Laventhol's right to bring third-party actions against the settling defendants so that no unfairness to Laventhol would result from the settlement (71a).

Thereafter, Laventhol served a Third-Party Complaint against nine of the settling defendants seeking contribution and indemnification (131a *et seq.*) and Allen in turn asserted third-party counterclaims against Laventhol (144a *et seq.*). The Court below, after a bench trial, dismissed Allen's counterclaims and allowed Laventhol to recover contribution from Allen. The Court found, among other things, that Allen, through its employee Lee Meyer, had knowledge of the character of the misleading representations in question and participated in disseminating them and certain other materials which the Court found to be "if not blatantly false . . . plainly misleading." The Court held, accordingly, that Allen was *in pari delicto* with Laventhol.

This case was tried from October 15, 1973 through October 29, 1974 and the opinion of the Court was filed on May 29, 1974 and is reported at 378 F. Supp. 112.

Summary of Argument

I.

Laventhol's third-party claim against Allen for contribution to that portion of the judgment rendered against Laventhol is fully preserved under applicable principles of federal and state law. Laventhol's claim for con-

tribution against Allen is grounded in a line of federal decisions which have held that the right of contribution should be allowed in order to promote the policies of deterrence underlying the federal securities laws. Additionally, state law supports Laventhol's contribution claim against Allen for that portion of the *Herzfeld* judgment based on common law fraud and Section 352-c of the New York General Business Law. The conditional voluntary dismissal in December, 1971 of all defendants except Laventhol expressly reserved the right of Laventhol to bring third-party actions for contribution against the settling defendants.

II.

Upon a thorough consideration of the issue of damages, the apportionment thereof, Laventhol's right to contribution from Allen, and the effect of the 1971 settlement, if any, the District Court correctly awarded to Laventhol contribution from Allen in an amount commensurate with Allen's liability for wrongdoing. The Court below correctly dismissed Allen's third-party counterclaims against Laventhol in light of the *in pari delicto* defense, and alternative grounds support that dismissal.

POINT I

Both Federal and State Law preserve Laventhol's third-party claim against Allen for contribution.

Analysis of Laventhol's third-party claim against Allen for contribution to the judgment rendered in *Herzfeld* necessarily involves an examination of the law of contribution under the federal securities laws, § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 79j(b) (1970) and Rule 10b-5, C.F.R. § 240.10b-5 (1973), as well as state law con-

cerning contribution for common law fraud and liability under New York General Business Law § 352-c (McKinney's 1968).

It is axiomatic that, where federal law does not preempt parallel state claims, a federal district court will apply the federal substantive law to federal questions and is "bound to apply state law" to pendent state claims. *United Mine Workers* v. *Gibbs,* 383 U.S. 715, 726 (1966); see also *Sola Electric Co.* v. *Jefferson Co.,* 317 U.S. 173, 176 (1942); *Erie R. Co.* v. *Tompkins,* 304 U.S. 64, 78 (1938). Given the dual federal and state law predicates of the *Herzfeld* judgment, it is necessary then to parse the applicable federal and state law.

A. Under federal law, a prior settlement does not bar a non-settling defendant's claim against settling defendants for contribution.

That there is a federal right of contribution accorded defendants found liable under § 10(b) is clear: The leading Second Circuit case to imply a right to contribution is *Globus* v. *Law Research Service, Inc.,* 318 F. Supp. 955 (S.D.N.Y. 1970), *aff'd,* 442 F.2d 1346 (2d Cir.), *cert. denied,* 404 U.S. 941 (1971). In *Globus,* purchasers of securities instituted suit against a corporation, its president and its underwriter for alleged violations of § 17(a) of the 1933 Securities Act, § 10(b) of the 1934 Act and for common law fraud. In a trial to a jury, the three defendants were found jointly and severally liable under the federal securities laws. Nevertheless, after trial, the underwriter paid plaintiffs the full amount of the judgment, reserving any rights it might have to contribution from the co-defendants. Granting the underwriter's motion seeking pro rata contribution, the district court noted that "the general drift of the law today is toward the allowance of contribution among joint tortfeasors." *Id.* at 957. Fur-

ther, the court stressed the policy of deterrence to be served by ensuring that no tortfeasor escapes his liability for securities fraud:

> "[A]llowing such means of absolution would dilute the deterrent impact of the securities laws, which seek 'to encourage diligence, investigation and compliance with the requirements of the statute exposing issues and underwriters to the substantial hazard of liability for compensatory damages'. . . . [T]he mode of escape sought by [defendants] is objectionable. . . . They may not effectively nullify their 'liability for compensatory damages' by leaving the whole of the burden to the more prompt and diligent party with which they have been cast in joint and several liability." (318 F. Supp. 958)

A right to contribution in § 10(b) cases was also found to exist in *deHaas* v. *Empire Petroleum Co.*, 286 F. Supp. 809 (D. Colo. 1968), *modified on other grounds*, 435 F.2d 1223 (10th Cir. 1970), where the court said:

> "Section 10(b) does not expressly allow contribution among wrongdoers, since civil liability under that section has been implied by the courts. However, those sections of the Securities Exchange Act which expressly provide for civil liability contain express provisions for contribution among intentional wrongdoers. Since the specific liability provisions of the Act provide for contribution, it appears that contribution should be permitted when liability is implied under Section 10(b)." (286 F. Supp. at 815-16)

The policy of deterrence served by allowing contribution has repeatedly been emphasized in other federal court

decisions. In *Altman* v. *Liberty Equities Corp.*, 54 F.R.D. 620 (S.D.N.Y. 1972), a class action brought under the securities laws, the court considered this policy paramount to the strong judicial policy favoring settlements. Accordingly, the court refused to approve a bar to contribution contained in a stipulation of settlement proposed by three of 12 defendants. In rejecting the bar, the court said:

> "Both *Globus* and *deHaas* make it clear that this right to contribution is federal . . . . [I]t can be said that the objecting defendants presently have sufficient rights in their potential claim for contribution that a bar thereof would be prejudicial to their interests. Put differently, since no one can now be certain that this case will not go to judgment, and because federal law recognizes the right to contribution in cases of this kind, these are sufficient grounds to require this court to refrain from barring the non-settling defendants from such rights at this time." (54 F.R.D. at 625)

In *Liggett & Myers, Inc.* v. *Bloomfield*, 380 F. Supp. 1044 (S.D.N.Y. 1974), another federal securities case, impleaded third-party defendants argued there was no right to contribution absent a joint judgment. The court, however, gave short shrift to this argument, stating:

> "[T]he sound policy reasons for allowing contribution from jointly liable co-defendants—to deter violation of the securities laws and prevent violators from escaping unpunished—are equally applicable to third-party defendants, who may otherwise escape liability because, for some reason, the plaintiff chose not to sue them. The fact that they are not named in the original action should not insulate them from liability for contribution to joint tort-feasors who

are sued by an aggrieved party." (380 F. Supp. at 1046)

Further, in *Alexander & Baldwin, Inc.* v. *Peat, Marwick, Mitchell & Co.*, 385 F. Supp. 230 (S.D.N.Y. 1974), the court said:

> "Because of the deterrent policy of the securities laws, even intentional tortfeasors may obtain contribution so that other tortfeasors will not escape liability. This purpose will be served if defendant tortfeasors are allowed to implead any other tortfeasors involved in the fraud." (385 F. Supp. at 238).

Altman, Liggett & Myers, and *Alexander & Baldwin*—these cases reaffirm that preservation of the right to contribution must be a major concern in federal securities fraud cases lest the very basis of the federal securities laws themselves be undermined. See also *Tucker* v. *Arthur Andersen & Co.*, [1973-74 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,544 (S.D.N.Y. 1974); *State Mutual Life Assurance Co. of America* v. *Arthur Andersen & Co.,* 63 F.R.D. 389 (S.D.N.Y. 1974).

The federal policy favoring contribution among codefendants is also reflected in Rule 41(a) of the Federal Rules of Civil Procedure which governs the availability of voluntary dismissal of claims. The rule provides in pertinent part as follows:

> "(2) By Order of Court. . . . an action shall not be dismissed at the plaintiff's instance save upon order of the court and upon such terms and conditions as the court deems proper. . . . Unless otherwise specified in the order, a dismissal under this paragraph is without prejudice."

Rule 41(a)(2) directly governs judicial determinations of whether partial compromise and settlement with some defendants will be allowed when such would bar remaining defendants from seeking indemnity or contribution from the settlors. *Altman* v. *Liberty Equities Corp.*, 54 F.R.D. 620, 623-24 (S.D.N.Y. 1972).

Altman, previously discussed for its emphasis upon the federal policy underlying contribution, also makes clear that settlements cannot foreclose the rights of objecting defendants. Thus the court in *Altman* stated:

> "[W]hile there is a policy in favor of settlements . . . there can also be no doubt that the non-settling defendants have a right to make cross claims . . . and to seek contribution in cases brought under § 10(b) of the Securities & Exchange Act. . . . Furthermore, while there are cases holding that less than all of several jointly liable defendants may be dismissed on plaintiff's motion, . . . none of the cases so holding under federal law involve a bar of contribution or cross claims." (54 F.R.D. at 623) (Citations omitted.)

And further the court stated:

> "In cases in which voluntary dismissal of less than all defendants has been allowed, the courts have noted that the remaining defendants will still be able to preserve their rights, as by filing third party complaints." (54 F.R.D. at 624) (Citations omitted.)

Other cases applying Rule 41(a)(2) have settled that a federal court will not approve a partial settlement where rights of objecting defendants will be prejudiced thereby. *Slotkin* v. *Brookdale Hospital Center*, 18 Fed. Rules Serv.

2d 1066 (S.D.N.Y. 1974); *see also Société Internationale Pour Participations Industrielles et Commercielles, S.A.* v. *Kennedy,* 7 Fed. Rules Serv. 2d 822 (D.D.C. 1963). Dismissal under Rule 41(a)(2) then is within the absolute discretion of the trial judge, who, pursuant to the provisions of the rule, may condition the dismissal "upon such terms . . . as the court deems proper."

In *Muth* v. *Dechert, Price & Rhoads,* [1974-75 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 95,030 (E.D. Pa. 1975), the court restated the principle that settlement and release of one tortfeasor prior to judgment does not preclude a subsequent claim for contribution by another tortfeasor. There, plaintiff shareholders brought a class action against a law firm, an accounting firm and an individual attorney as co-defendants and alleged § 10(b) and Rule 10b-5 violations arising out of the sale of stock. Defendants impleaded other individuals and corporations named as defendants in *Oberholtzer,* a separate action involving the same sale of stock. And these third-party defendants filed a motion to dismiss, maintaining as one of two grounds for dismissal that their prior settlement in *Oberholtzer* was a bar to third-party plaintiffs' claim for indemnity and contribution. Dismissing the third-party complaints without prejudice on the ground of insufficient pleadings, the district court nevertheless held:

> "[C]laims for contribution or indemnity against . . . Defendants, if properly set out in adequate Third-Party Complaints, would not be barred by the settlement in the *Oberholtzer* case." (*Id.* at 97,603)

The court also noted that the order approving the settlement in *Oberholtzer* was expressly entered without prejudice to the third-party claims of non-settling *Oberholtzer* defendants—a stipulation also present in Judge Palmieri's

approval of the *Herzfeld* settlement (71a). As the court stated in *Muth*:

> "*A fortiori,* if the claims of the non-settling defendants in the *Oberholtzer* case are preserved by the settlement, the rights of defendants in the present case . . . cannot be prejudiced by that settlement." (*Id.* at 97,602-97,603)

The claims of the *Oberholtzer* defendants survived the settlement according to the express stipulation to that effect. So too did Laventhol's contribution claim against Allen survive. Further, the principle of fairness articulated by the *Muth* court is fully pertinent to Laventhol: ". . . the rights of defendants . . . cannot be prejudiced by . . . settlement." Thus, *Muth* falls into line with other federal decisions which consistently evidence protection of the rights of non-settling defendants.

Sabre Shipping Corp. v. *American President Lines, Ltd.*, 298 F. Supp. 1339 (S.D.N.Y. 1971), cited by Allen in opposition to Laventhol's contribution claim, is simply inapposite. *Sabre* was a case arising under federal antitrust laws. In holding that plaintiff's partial settlement extinguished all claims to contribution of non-settling defendants and settlors *inter sese,* the court premised its decision on the fact that "no provision in the antitrust statutes provid[es] for contribution . . . ." (298 F. Supp. at 1345) Moreover, the court specifically refused to imply a right to contribution by analogy to the contribution right under the 1933 and 1934 Securities Acts. Noting the express provisions for contribution in the federal securities laws, the court stated:

> "All that this demonstrates is that Congress, aware of the rule against contribution, saw fit to provide for it explicitly in the securities statutes but not in the enforcement of antitrust laws which domi-

> nate so much of our litigation, and that no such right should be implied." (298 F. Supp. at 1345)

Clearly, then, the issue of the effect of settlement in *Sabre* was tangential to the thrust of the court's decision: Since the court refused to imply a right to contribution in antitrust cases at all, it of course refused to apply such a right after plaintiff had settled with some of the defendants.

Herzfeld, on the other hand, is a case arising under federal securities laws, and the right to contribution has been both expressly preserved in the statutes and has been implied by the courts. *Globus* v. *Law Research Service, Inc., supra; deHaas* v. *Empire Petroleum Co., supra.* Moreover, both *Muth* v. *Dechert, Price & Rhoads, supra,* and *Altman* v. *Liberty Equities Corp., supra,* make clear that Laventhol's claim to contribution from Allen was not prejudiced by the 1971 settlement to which it was not a party.

In *Herzfeld,* Judge Palmieri followed established precedent in carrying out the mandate of Rule 41(a)(2) when he conditionally allowed voluntary dismissal as to the settling defendants in December, 1971. Allen argues that Judge Palmieri's order merely addressed procedural matters and was not a decision on the merits of Laventhol's third-party action. Laventhol does not contend that Judge Palmieri's conditional order "created" rights in Laventhol which were not already there. However, the facts surrounding the settlement do clearly show that Judge Palmieri was concerned that rights already accruing to Laventhol not be extinguished by the settlement.

On November 18, 1971, Judge Palmieri vacated a Dismissal Order which he had signed on November 5, 1971. In an endorsed memorandum he wrote:

> "Order set aside because counsel for the defendant Laventhol, Krekstein, Horwath & Horwath was

not requested to sign the stipulation or given notice that such stipulation would be submitted to the Court. See Rule 41 F.R.C.P." (65a)

In subsequent proceedings, counsel for Allen and three other defendants submitted an affidavit in support of dismissal without conditions (81a). In that affidavit, Allen's counsel maintained that Laventhol would not be prejudiced by the settlement and concurrent dismissal as follows:

> "Laventhol already has, under the Federal Rules of Civil Procedure, the right now or later to serve a third-party complaint. . . ." (82a)

As that statement indicates, counsel was well aware that preservation of Laventhol's right to contribution was at stake. The instant lawsuit was then hardly six months from its commencement. The naked pleadings were all that were before the court and discovery had only recently then begun. Indeed, trial would not be had until almost two years later, in October, 1973.

It was with this background that Judge Palmieri allowed voluntary dismissal as to the settling defendants but set down the following Order with conditions:

> "This settlement between the plaintiff and all the defendants except the Laventhol firm, is hereby approved after argument. Since counsel agree that an amended complaint, which Mr. Haimoff, counsel for plaintiff, expects to serve within 20 days, will set in motion the procedural steps whereby the defendant Laventhol, if it is so advised, can bring third-party actions against any of the settling defendants, there is no unfairness to the objecting defendant Laventhol." (71a)

As the Order indicates, Laventhol's procedural right to bring claims against "any of the settling defendants" was expressly reserved. Thus Laventhol is in full agreement with counsel for Allen that Judge Palmieri's approval dealt with "procedural" matters; the Order reserved Laventhol's procedural right to assert its substantive claims for contribution and indemnity by way of third-party actions. Now comes Allen complaining that the procedural right reserved by Judge Palmieri should be extinguished because Allen does not like the substantive result reached by Judge MacMahon's decision on the contribution issue. In other words, unhappy with the result which Allen's stipulation has brought to its door, Allen seeks to undo the portion of the decision which vindicates Laventhol's right to assert a claim for contribution. At this late date, Allen should not be heard to complain that the Court's decision on the merits is barred by the prior settlement.

B. Under applicable state law, Laventhol's claim to contribution against Allen for Laventhol's pendent state law liability was not extinguished by the 1971 settlement.

The doctrines of *United Mine Workers* v. *Gibbs,* 383 U.S. 715 (1966), and *Erie R. Co.* v. *Tompkins,* 304 U.S. 64 (1938), require application of state law to state claims interposed in federal courts. The state law governing the instant contribution claim based on common law fraud and § 352-c liability is laid down in *Dole* v. *Dow Chemical Co.,* 30 N.Y.2d 143, 282 N.E.2d 288 (1972), where the Court of Appeals held that, whether pursued in a separate action or by third-party practice within the original action, an apportionment of damages could be had by the party cast in damages above its equitable share. Codified and clarified in newly enacted New York CPLR § 1401 (McKinney's

1974),* the *Dole* right to apportionment has been characterized as a "substantive right." *New York Elec. & Gas Corp.* v. *Waldron,* 72 Misc. 2d 78, 79, 338 N.Y.S.2d 248, 250 (Sup. Ct. Broome Co. 1972).

Moreover, the New York Court of Appeals has given retroactive effect to *Dole*: In *Kelly* v. *Long Island Lighting Co.,* 31 N.Y.2d 25, 29 n.3, 286 N.E.2d 241, 243 n.3 (1972), the Court mentioned in a footnote: "We, of course, in our review of pending appeals, give effect to the law as it exists at the time of our decision." Then, in *Rodgers* v. *Dorchester Associates,* 32 N.Y.2d 553, 563, 300 N.E.2d 403, 408 (1973), the Court applied *Dole* to a decision tried before *Dole* was decided. And most recently in *Codling* v. *Paglia,* 32 N.Y.2d 330, 344, 298 N.E.2d 622, 629-630 (1973), the Court reiterated, "*Dole* appl[ies] to pending cases." Thus *Dole* and its codification in New York CPLR § 1401, effective September 1, 1974, are clearly applicable to Laventhol's contribution claims in *Herzfeld* to the extent they turn on state law.

Lower courts that addressed the settlement issue after *Dole* uniformly held that the right to contribution may be asserted by one tortfeasor against another tortfeasor who has settled and obtained a personal release. *Williams* v. *Town of Niskayuna,* 72 Misc. 2d 441, 339 N.Y.S.2d 888 (Sup. Ct. Schenectady Co. 1972); *Evans* v. *City of New York,* 72 Misc. 2d 216, 338 N.Y.S.2d 538 (Sup. Ct. Kings Co. 1972); *Michelucci* v. *Bennett,* 71 Misc. 2d 347, 335 N.Y.S.2d

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* § 1401. Claim for contribution.

Except as provided in section 15-108 of the general obligations law, two or more persons who are subject to liability for damages for the same personal injury, injury to property or wrongful death, may claim contribution among them whether or not an action has been brought or a judgment has been rendered against the person from whom contribution is sought.

967 (Sup. Ct. Washington Co. 1972). In *Michelucci,* the plaintiff had settled its action with two of three defendants during the course of the trial and had reserved its rights to continue against the remaining defendant. Thereafter, the defendant impleaded the settlors for contribution, and the third-party defendants filed a motion to dismiss on the ground that plaintiff's general release of them was a bar to a third-party action. Summarily dismissing this argument, the court stated:

> "This argument fails to recognize that the plaintiff . . . is not asserting any additional claim against either [third-party defendant]. The [third-party] plaintiff . . . is not a party to the release nor bound by its terms. . . ." (71 Misc. 2d at 348-49, 335 N.Y.S.2d at 969-70) (Interpolation added)

In *Williams, supra,* the impleaded defendant argued that his prior release obtained from the plaintiff was a bar to a third-party action. Here, too, the court denied third-party defendant's motion to dismiss on the grounds "that a settlement between the plaintiff and the third-party defendant is not binding on [the remaining defendant]." (72 Misc. 2d at 442, 339 N.Y.S.2d at 889)

Moreover, in *Codling* v. *Paglia,* 38 A.D.2d 154, 327 N.Y.S.2d 978 (3d Dept. 1972), *aff'd,* 32 N.Y.2d 330, 298 N.E.2d 622 (1973), the Court of Appeals suggested that the result reached by lower courts, as discussed above, would follow from the logic of the *Dole* decision. In *Codling,* plaintiffs, having sustained injuries in a two-car collision, brought suit against Paglia, the owner-driver of the other car, and Chrysler, the manufacturer of Paglia's vehicle. Paglia, in turn, cross-claimed against Chrysler for *Dole* apportionment. Before trial, however, plaintiffs settled with Paglia. Without a reservation of rights for Paglia to

claim against Chrysler, the court approved the settlement and severed Paglia's cross-claim for later joinder with Paglia's separate action against Chrysler.

Affirming the Third Department's reversal of the judgment for Paglia on his cross-claim, the Court of Appeals refused to apply the principle of *Dole* to undo the settlement but only because to do so would negate the intent of the parties thereto:

> "The participation of the parties in this settlement was completed prior to our decision in *Dole.* In our view it would be inappropriate on these facts to undo what has been done and, on the basis of the present law, to nullify actions taken by the parties in reliance on the law as it then stood." (*Id.* at 344, 298 N.E.2d at 630)

Clearly, *Codling* stands for the proposition that courts should respect the intent of settling parties and accord recognition to party reliance "on the law as it then stood." The record herein evinces that settling parties in *Herzfeld* did not intend that the settlement would extinguish Laventhol's third-party claims. To the contrary, parties to the stipulation were given the clear understanding by Judge Palmieri that "defendant Laventhol . . . can bring third-party actions against any of the settling defendants . . . ." (71a)

This express reservation of the rights of defendant is in contrast to the *Codling* settlement which did not reserve Paglia's contribution claim against Chrysler. Further, Paglia unilaterally bought his peace with plaintiffs. Laventhol on the other hand was an objecting defendant to the *Herzfeld* settlement and was never given the opportunity to enter into settlement negotiations so it might thereby reduce its potential liability. It was for this very

reason that Judge Palmieri vacated the Dismissal Order of November 5, 1971 (65a).

Allen cites New York General Obligations Law § 15-108(b) (McKinney's 1974), which did not become effective until September 1, 1974, in support of its argument that a non-settling defendant may not seek contribution from a settling defendant. That section of the General Obligations Law, which provides that "[a] release . . . to one tortfeasor . . . relieves him from liability to any other person for contribution," should not be applied to the *Herzfeld* settlement, which predates the statute. Section 15-108(b) is an entirely new addition to the predecessor statute, which was first enacted in 1972—after the *Herzfeld* settlement. The original New York General Obligations Law § 15-108, effective September 1, 1972, was an attempt by the Legislature to clarify the effect of settlement and release for the post-*Dole* plaintiff. Captioned "Effect of Release of or Covenant Not to Sue Tortfeasors," old § 15-108 said nothing about the rights of defendants.

Moreover, the fact that legislation was required, in the form of § 15-108(b) to achieve the result here sought by Allen, persuasively demonstrates that such a result did not flow from the law prior to its enactment. That pre-existing law governs here.

Both the 1972 and 1974 versions of § 15-108 are silent as to their application to settlements concluded prior to the effective dates of those statutes. The courts have uniformly declined to apply the 1972 version of § 15-108 with retroactive effect. *Jordan* v. *Westhill Central School District*, 42 A.D.2d 1043, 348 N.Y.S.2d 620 (4th Dept. 1973); *Williams* v. *Pitts*, 40 A.D.2d 1057, 338 N.Y.S.2d 969 (3d Dept. 1972). Nor has any New York court applied amended § 15-108 retroactively.

The net result of the foregoing, then, is as follows: neither the former nor the amended G.O.L. §15-108 applies

to the 1971 *Herzfeld* settlement under any conceivable legal theory or case law authority. To apply retroactively those statutes would be manifestly unfair to Laventhol who relied upon the law at the time the settlement was consummated and saw to it that its rights to contribution were expressly reserved in reliance on the law at the time of the settlement.

POINT II

The District Court correctly awarded contribution to Laventhol in an amount commensurate with Allen's liability and correctly dismissed Allen's third-party counterclaims against Laventhol.

Allen complains that Judge McMahon erroneously allowed contribution to Laventhol in the amount of $76,500 with costs and interest so that Allen now must pay more than its fair share. Simply put, given the evidence adduced at trial and Judge McMahon's consideration of the issue of damages, the apportionment thereof, and the effect, if any, of the 1971 settlement, it becomes abundantly clear that the Court intended to tack on to Allen's liability an additional amount over and above any amount it paid at settlement.

Giving effect to the deterrent purpose underlying the federal securities laws, the Court found Allen to be responsible for Herzfeld's remaining damages in a measure equal to Laventhol and thus apportioned the damages to reflect this conclusion. Herzfeld originally sued for a total amount of $510,000 in damages and the 1971 settlement by 11 defendants, including Allen, was for $357,000, leaving the amount of $153,000 still due to Herzfeld. The Court decided that Allen and Laventhol should each pay one-half of the remaining amount due to Herzfeld, that is, $76,500 each.

The record is replete with evidence supportive of the Court's conclusion that Allen should bear the brunt of Herzfeld's financial loss. The state of the record on Allen's participation in the misrepresentations—which Laventhol contends constitute grounds not merely for contribution but, more, for exculpation—is briefed in Laventhol's brief as defendant-appellant (pp. 23-28). It need not be rehearsed here. In brief compass, that record justifies fully the Court's findings of Allen's guilt.

Thus even if this Court should find that the Laventhol report was misleading, it will also find in the record that Allen, through its representative Lee Meyer, actively participated in the misrepresentations. When Firestone Group became aware of Laventhol's planned conservative accounting treatment of the Monterey transactions, Richard Firestone ("Firestone") objected strenuously and argued that unless all the income was so reported, Allen would be very upset (940-941a). Firestone testified that Meyer agreed that all the profit from the Monterey transactions should be included in income (803a; 805a). Meyer, himself, testified that he wanted to be sure that the profit was taken into the income statement because the transactions had actually occurred (715-716a).

Firestone Group met at the New York offices of the attorneys for Allen in the private placement on or about December 15, 1969, to confer on the Laventhol report. When the Laventhol report and the audited financial statements were shown to Robert Feinberg, of Counsel to Firestone Group,* he was disconcerted because the audited statements

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* The Court below mistakenly refers to Feinberg as Allen's lawyer rather than Firestone Group's. The lapse is not significant because the point of Laventhol, the Court and the evidence is that from the discovery on December 15 of the disconcerting audit result, Firestone and Allen worked in concert to save the offering by dissipating the negative impact of the Laventhol report through falsely reassuring materials sent to the purchasers.

did not confirm the projections which appeared in the previous unaudited statements. The Laventhol report showed "substantially less earnings than what had been projected for the period" (977-978a). Feinberg testified that he felt that without further explanation to the investors, the private placement should not close (969a; 972a).

Such concern was generated at the meeting that Meyer was immediately summoned to join the meeting and the assembled group called the California offices of Laventhol via speaker phones at both ends to discuss what was now considered a problem. No representative of Laventhol was present at the meeting. During the telephone conversation, Messrs. Chazen and Lipkin at Laventhol were questioned regarding Meyer and Firestone's contention that all of the profit from the Monterey transactions should be taken into income (860a; 863a; 866-867a). Nevertheless, Laventhol refused to alter its report, opting for the more conservative accounting treatment.

The Laventhol report, which prompted Firestone Group's attorneys to caution against closing without some further explanation to the investors as to the differences in the consolidated and audited statements, was not altered. Yet Allen, aware of these facts, still closed the private placement on December 16, 1969, receiving $200,000 as a fee.

In short, Allen went forward with the deal in spite of the discrepancies between the unaudited and audited statements. Allen also actively participated in writing an explanation of the Laventhol report (31e *et seq.*). It was this explanation composed by Firestone, Meyer and Feinberg when Laventhol refused to change its report which mate-

rially influenced the investment decisions of the purchasers —one of whom, of course, was Herzfeld, who read it with care but did not read the Laventhol report. The Court fully reviewed the evidence in arriving at its judgment on the relative culpability of Allen:

> "There is also evidence to the effect that Allen, through Meyer, participated in discussions leading to the preparation of a letter, dated December 16, 1969, which both minimized and obscured the differences between the audited and unaudited financial statements."
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> * * *
>
> "The letter, after describing the discrepancies between the conflicting financial statements, stated that 'none of these changes have resulted or will result in an adverse change in the financial condition or the results of our operations.' Obviously, the letter was intended to still investors' doubts about the private placement and convince them that the differences between the unaudited and audited financial statements were of no consequence."
>
> "Since the net income figure in the unaudited statements was nearly five times greater than the net income figure in the Laventhol audited report, the statement in the letter, if not blatantly false, was plainly misleading. Thus, we find that Allen, through Meyer, knowingly misled investors by minimizing the material discrepancies between the audited and unaudited statements."
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> * * *
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> "Meyer, in his role as one of three directors of FGL, was thoroughly familiar with FGL's operation, and, although he testified that he was not active in the day-to-day management of the company,

he did attend board meetings, review financial statements and observe operations. There can be no question that he was familiar with the Monterey transaction and its importance in FGL's total financial picture. We think the facts support the inference that he knew whether the units were a sound investment.

* * *

"Meyer also testified that he in no way attempted to influence Laventhol. He first said that he questioned Lipkin about the financial statement on December 15, 1969, when Lipkin personally delivered it to New York. After Meyer left the stand, Lipkin testified that his time sheet showed that he had not been in New York on December 15, 1969. Moreover, he was positive that he had not been in New York on that date because he had not been there for thirty-five years except to attend a hearing before the Attorney General of New York some time subsequent to December 15, 1969. Confronted with Lipkin's testimony and the time sheet Meyer changed his story. He conceded that his only conversation with Lipkin was by telephone and explained that he was confused in his earlier testimony about meeting him in New York on December 15.

* * *

"We find Meyer's demeanor, his monetary motive to color the offering, his agreement with Firestone's position on the report, his participation in the preparation of the minimizing letter, and his changed story about meeting with Lipkin in New York on December 15, 1969 cast considerable doubt on the reliability of his testimony and the accuracy of his recollection.

"In light of Meyer's inside knowledge of FGL's operation and, particularly, the Monterey transaction, we conclude that he had knowledge of the misleading nature of the report yet failed to disclose material facts to correct its misleading character. Allen is chargeable with knowing participation with Laventhol in misrepresentation and fraudulent nondisclosure of material facts. As underwriter of the private placement, Allen, no less than Laventhol, had a duty to reveal all the material facts needed by investors to enable them to make an intelligent investment decision. Allen plainly failed to fulfill its duty of full and fair disclosure to investors. Worse, had Meyer succeeded in his efforts to inflate the reported income in the audited report, the report would have become even more misleading than it was." (378 F. Supp. at 133-135)

These findings by Judge MacMahon fairly summarize the proof adduced at trial. Having had full opportunity to observe the demeanor, recantations and evasions of Allen's witnesses, including Meyer, Judge MacMahon correctly concluded that if Laventhol was responsible for Herzfeld's remaining damages, Allen was even more so. Thus he correctly awarded contribution to Laventhol in an amount commensurate with Allen's liability and correctly dismissed Allen's third-party counterclaims against Laventhol.

The correctness of the dismissal of Allen's counterclaims becomes clear upon consideration of the facts. The

Court below found Allen to be *in pari delicto* with Laventhol because of the conduct of Allen:

> "Allen, moreover, not only attempted to make the [Laventhol] report more misleading, but participated in minimizing the discrepancies between the audited and unaudited reports. Allen and Laventhol are, therefore, *in pari delicto.*" (378 F. Supp. at 137)

Laventhol agrees fully with the legal analysis of the Court below in regard to the *in pari delicto* defense and further contends that, even if the Court below had not so held, Allen's counterclaims would still be barred. Allen's counterclaims are based solely on purported assignments of claims to Allen in 1971 when Allen purchased Firestone Group units, or fractions thereof, from Allen customers pursuant to written agreements (450-457e). Allen, however, failed to prove at trial that such assignments did in fact occur. Only one of the written agreements contains language of assignment of claims.

Allen's attorney, Duff, testified that Allen negotiated for the purchase of all or portions of the units which the owners had purchased in the original private placement (639-640a). A series of eight documents were offered (450-457e) as reflecting these acquisitions by Allen; but of these eight documents, seven contain no reference whatsoever to any assignment of claims to Allen. Duff testified that all were prepared by him under his supervision and that the seven documents fairly and accurately reflected the transactions (660-661a). Moreover, Duff also admitted that in some of the transactions, the selling parties retained interests by way of common stock which Allen did not purchase (662-663a).

The only other evidence tendered to prove the assignments was parol evidence, which was of course insufficient to vary the clear terms of the written instruments. The law is well-settled that where there is a writing which fairly and accurately reflects the transaction, that writing speaks for itself and requires no interpretation or construction since the writing gives rise to a presumption that it expresses the whole of the agreement. 10 *N.Y. Jur., Contracts* §§ 189, 209 (1960); *Restatement of Contracts,* Ch. 9, §§ 235, 239(1) and Comments (Tent. Draft No. 5, 1970).

Apart from the technical defects in Allen's proof of the putative oral assignments, Allen failed to present a credible account of any assignment of claims. Initially, counsel for Allen did not even attempt to elicit testimony of any such oral assignment, merely inquiring of Mr. Duff whether it "was . . . *part of the understanding* in the 1971 [Allen] purchase that they were obtaining all of the rights of the purchasers to sue under those agreements" (646a). Counsel continued this formulation in his offer of proof (647a).

Only later in the trial did Allen's counsel inquire about the receipt of "oral assignments of all rights, including the right to sue." At trial no effort was made to lay a foundation for the seven conversations in which these oral assignments purportedly took place. There was no proof of who made the oral assignments (particularly in the case of the four alleged assignors that were not individuals but partnerships or corporations); there was no evidence of who received the "oral assignments"; and, furthermore, there was no explanation of why language of assignment was not included in the written instruments of conveyance.

Those omissions become even more glaring in the light of three additional uncontested facts:

(1) The first written confirmation of conveyance, from Elliot Hyman to Allen, dated February 25, 1971, contained language confirming assignment. All of the other seven written instruments confirming conveyance of rights in units are dated *after* the Hyman document. It would seem reasonable that if assignments of the right to sue had in fact been considered by the parties, language like that in the Hyman document would have been included.

(2) The seven later written instruments were prepared by Duff, Allen's attorney, and were described by him as fully and fairly expressing the transactions which he had negotiated. If assignments had in fact been part of "the understanding," why did Allen's lawyer fail to include language protecting Allen's rights in the instruments he otherwise so carefully prepared?

(3) Several of the confirmations relate to fractional interests in units or, in one case, to securities received by the investor as a result of treatment accorded a fraction of his unit by the California bankruptcy court. It is highly unlikely that, as to these conveyances of less than full units, assignments of fractional parts of the right to sue would have been conveyed to Allen while other fractional parts were retained by the seller.

Finally, it must be remembered that in order to believe Allen's version about these oral assignments, this Court must imagine that Duff had a series of intermittent conversations from March to December of 1971, during which he punctiliously elicited an oral assignment of the right to sue but then completely omitted mention of the agreements from the writings he prepared to fully and fairly reflect the transactions.

In summary, the record is barren of any competent testimony that Allen acquired any such claims as the persons from whom they purchased may have had. The failure of Allen to prove the existence of assignments, written or oral, is fatal to Allen's counterclaims.

Even if the assignments had been proved by Allen at trial, the counterclaims still are legally deficient due to releases of all claims concerning the transactions at issue. (357-368e). Those releases clearly absolve Laventhol from any liability. The law which was effective in 1971 when those releases were given, Section 15-104 of the General Obligations Law of New York (McKinney's 1964), provides in pertinent part as follows:

> "Subject to the provisions of section 15-103, the obligee's release or discharge of one or more of several obligors, or of one or more of joint, or of joint and several obligors shall not discharge co-obligors, against whom the obligee in writing and as part of the same transaction as the release or discharge, expressly reserves his rights; . . ."

The Practice Commentary to this section states:

> "The section appears to adopt the line of decisions which requires the reservation of rights to be a part of the written transaction of release and rejects oral reservations." (23A McKinney's at 575)

Since the releases simply did not reserve any rights, the law clearly released Laventhol, as well as Allen. Therefore, this Court must, as did the Court below, reject the contention that Allen could, even if assignee of the original claims, make valid claims against Laventhol, since they were extinguished as a matter of law by the releases.

Finally for Allen's counterclaims based on purported assignments to withstand dismissal, Allen was required to prove at trial all the elements of the alleged fraud that its assignors would have had to prove if they had brought suits on those claims. Again it is basic that an assignee stands in the shoes of its assignor. Thus Allen was compelled to show that each of their assignors relied on the Laventhol report, a task which Allen was unable to perform.

The record is almost silent on the issue of the supposed assignors' reliance on the Laventhol report, an essential element prerequisite to the proof of fraud. Allen's witness, Goodman, initially gave the ritualistic testimony that he read and relied on the Laventhol report. However, he later acknowledged that he had been influenced in his investment decision "to a very great degree" on Allen's "putting together this deal" (686-687a). And he further admitted that he did not receive the Laventhol report until after the closing. Goodman was the only alleged assignor who was offered as a witness by Allen and even his testimony indicates that his reliance was upon Allen and not upon the Laventhol statements which he received after his purchase. There is no evidence in the record that any of the other alleged assignors ever saw or heard of the Laventhol report, much less that they relied thereon. No inference of their reliance on the Laventhol report can be garnered from so profound a silence and neither can this Court sustain Allen's counterclaims in the absence of proof of reliance by the alleged assignors.

In sum, the dismissal of Allen's counterclaims against Laventhol was mandated by the law and the evidence and this Court should affirm the dismissal by the Court below.

CONCLUSION

If this Court should affirm the decision of the Court below, the Amended Judgment of the District Court should be affirmed as well in the respects stated herein.

Respectfully submitted,

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